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Target Questions

The Problem: The Role of the Board of Directors

Your board is in session, and has a particularly full agenda. The first item has to do with your expansion into the lumber business to serve member needs. You have purchased a good local lumber yard with a popular manager and a good volume of farmer business. The yard manager knows the lumber business thoroughly, but knows nothing about cooperatives. One of your directors moves that the lumber executive be kept on to run the yard as a department of the cooperative, and that he report directly to the board. The same board member also states that the cooperative can operate more efficiently by the exchange of labor and equipment between the lumber department and the grain and farm supply department.

Is there a problem here? If so, what action should your board take and what is the problem?

The next item on your agenda involves employee relations. One of the board members announces he has learned that a number of the cooperative's employees are dissatisfied with wages and working conditions. He moves that the president be empowered to appoint a committee of three directors to serve as a grievance committee to consider employee complaints in private sessions immediately prior to each board meeting.

Is this in accord with your understanding of the proper role of a board of directors? What action does your board take?

The same board member also moves that the board annually rehire and fix salaries for all employees. What action does your board take?

The next item on the agenda is discussion of plans for the coming annual meeting. The manager announces that he has already completed the plans, since he knew the directors were all busy men. His plans he then hands to the directors in printed form. They include the date, time and place, and provision for the official announcement consistent with the legal requirements. The manager has also planned the program, including business matters, entertainment and free meals for all who attend. His plan announces the composition of the nominating committee which he has selected, and outlines procedures to be used by the committee.

This is the first information the board has had about such plans. Does the manager's activity agree with your understanding of his proper role? What action should your board take?

The final item on the agenda relates to the annual audit. The manager, having previously selected an accounting firm to make the annual audit of the cooperative's books and records, has the report. He hands copies to each board member and then proceeds to analyze and discuss the auditing firm's report. Should your board take any action? If so, what?

At the conclusion of the meeting the manager speaks up:
"The next decade can be the most productive period in the history of your cooperative. But to make the most of your opportunities you need to plan ahead. I have prepared for your approval a list of basic objectives and goals to be reached in ten years, a statement of policy to guide us in reaching those goals, and a set of plans to guide our operations. I move that these objectives, goals, policies and operating plans be approved."

What issues are involved here? What action does your board take?

This board meeting illustrates the importance of a clear understanding of and respect for the separate and distinct roles of directors and hired management. It also suggests the problems that can arise when such understanding and respect are missing. In reaching decisions on the various questions raised, your board will need to consider the following:

1. To what extent should a board delegate authority to the manager to direct employee activities?
2. Under what conditions should a board undertake to make employee assignments?
3. Under what conditions should employees, other than the manager, report directly to the board?
4. Is there anything inherently wrong with having the board hire and set salaries for all employees?
5. Under what conditions should the manager make plans and commit the cooperative to spend money?

6. What is the accepted procedure for making the annual audit?
7. Is the board responsible for telling the manager the scope and content of his job?
8. Who usually sets policy and defines goals and objectives in a cooperative? Under what conditions is this not necessary?
9. What is the most desirable process for developing and implementing operating plans and projections?
10. To what extent should the manager participate in board meeting? Answer questions? Make suggestions? Make motions? Vote?

The Problem: Open Membership--Doctrine or Delusion?

Your board of directors is in session. Your treasurer has just finished his monthly report. It shows that the cooperative has had an operating loss every month for the past year. Inquiry from several directors reveals that one source of the loss is excessive costs for serving one of the newer members. Further inquiry reveals that this member is located at quite a distance from the cooperative plant causing extra trucking expense; that the quality of his production is low and thus expensive to grade and sell; and that his low volume made for the high per unit trucking and processing costs.

One director moves that the problem member be ousted from the cooperative at the close of the season and that his

membership fee be returned to him. The motion is seconded, and the president calls for discussion.

"I'm for the motion," declares one director. "His farm is too far away to be served efficiently, it costs us more to serve him, per unit, than to serve the rest of our members. His quality is poor and pulls down the average returns for the rest of us. And we don't need his volume anyway. We already produce just enough to satisfy the needs of our present customers."

"Well, I'm against it," observed another. "We all know that one of the basic cooperative principles is open membership. That means if someone wants to be a member we have to take him in. We can't throw him out as long as he obeys the bylaws."

At this point, the president speaks: "I think there's a better solution to our problem. If it costs more to serve this member because of the distance, quality and volume factors that have been mentioned, then we should adjust the charges to reflect those added costs. And as for not needing the volume, I think we should plan to expand our markets a little each year."

"I don't like that at all," said another. "I've always understood that one of the basic cooperative principles was equal treatment for all. If we charge one member more to haul his products than we charge another, that's not my idea of equal treatment."

The motion has been made and seconded. The discussion

has brought out some basic issues bearing on the problem.

What should the board's decision be?

In considering your answer, it may help you to ask yourself the following questions:

1. Are there any conditions under which a cooperative can have a closed or restrictive membership policy?
2. If so, are those conditions compatible with the principle of open membership?
3. Does treating all members alike mean equal charges for goods or services?
4. Can you think of a situation in which equal treatment could benefit some members at the expense of other members?

The Problem: The Effect of Mergers, Consolidations and Forward Integration on Member and Public Relations

Your board of directors is in session. After disposing of routine business, your president makes the following report: "Most of the legal details of our planned merger with XYZ Cooperative have been completed. But our joint merger committee tells me that some unexpected problems have developed. They want some suggestions from the two boards for solving the problems.

"The first problem involves employees. The committee wants to bring in a new man to manage the merged organization. But the manager of each of the present cooperatives thinks he should get the job. If we pick one of them, the other will be

unhappy. If we bring in a new man, they'll both be unhappy-- and so will some of the other employees who had hopes of moving up."

Based on your assumptions about the size and complexity of the merged organization, what action should the board take? Is employee morale a problem the board should be concerned with?

The president continues: "The second problem concerning the committee related to the public reaction to the planned merger. Our cooperative will become the headquarters for the new organization. But the Chamber of Commerce in the town where the XYZ Cooperative is located wants the headquarters to be there. And the XYZ bank is worried about losing the cooperative account when we merge. Also, some of the XYZ office employees don't want to move here."

Should the board be concerned about cooperative public relations? What actions can or should the board take to overcome the concern expressed above?

"The next problem," says the president, "has to do with the board of directors. We originally thought we should keep the new board to the same size as our present boards. That means half of us will no longer be directors. But several of the XYZ directors don't want to give up the prestige of being directors. In addition to the personal problem, this involves the wording of the articles of incorporation and bylaws. Frankly, the committee would welcome suggestions."

Can this problem be resolved? How? Is the board really responsible for making a decision under these special conditions?

The final problem the committee is currently struggling with, according to the president, is one of member relations. "Some of the members," he reports, "are afraid the new organization will be so big that the little individual member will lose control. And they don't like the idea of having to go clear across the county to get services that used to be close by. Some of our members are finding it hard to join hands with an organization we've competed with for the last twenty years."

Is there really a problem here? If so, whose problem is it? The board of directors? The manager? The merger committee?

What action should the board take?

There is a common element present in every one of the situations described by the president. As you consider what actions the board should take, it will help to have answers to the following questions in mind:

1. What is the element common to all the situations described by the president?
2. What is the single most important criterion in selecting a cooperative manager?
3. Is employee morale important to a cooperative?
4. What are some of the factors that contribute to good employee morale? To bad morale?

5. Can good public relations help a cooperative? How?
6. Is it necessary to keep all the directors happy?
If so, what are some of the ways this might be accomplished short of keeping them on the board?
7. Should members be kept informed of plans for and reasons for a proposed merger?
8. At what point in the negotiations should members be told what's going on? Should members participate in the discussions? If yes, why? If no, why not?

Problem:

The marketing coop you belong to had a gross business volume of \$5,500,000 this last year. Total expenses for the year were \$4,400,000. You and farmer Jones did exactly the same amount of business with the coop. In the exempt coops your total business was 2%, and in the non-exempt your total business was 3%. Total amount of common stock of your coop is \$6,000,000 of which you own 1/20.

In the space below show the calculations necessary for determining your coop's income tax return. Indicate the deductions available to the coop and the amount of each assuming first your coop is exempt and then non-exempt. Under each situation show the amounts both you and farmer Jones would receive in stock dividends, refunds, or both.

For each situation:

- Farmer Jones is not a coop member.
- The non-exempt coop pays patronage refunds to members only.
- The corporate tax rate is 50%.
- The board pays a 4% stock dividend.
- Farmer owns no stock.
- You and farmer Jones have income that puts each of you in the 40% IRS taxation rate.

Exempt

	<u>Your Share</u>	<u>Jones Share</u>
Patronage Refund	_____	_____
Stock Div.	_____	_____
Net Margin =	_____	_____

Deductions:

Coops Taxable Income =		
Taxes Paid by Coop =	_____	_____
Total Received	_____	_____

If you and Jones are typical of all members and customers of the coop and if we assume all have some tax rate, how many dollars of coops earnings go to IRS _____? What is percent of taxes paid on coop earnings _____?

Non-exempt

Your Share

Jones Share

Net Margin =

Deductions:

Coops Taxable Income =

Taxes Paid by Coops = _____

Total Received _____

If you and Jones are typical of all members and customers of the coops and if we assume all have same tax rate. How many dollars of coops earnings go to IRS _____? What is percent of taxes paid on coop earnings _____?

Who should run the cooperative - the board of directors or management?

Should a regional cooperative be centralized or federated?

How big should agricultural cooperative be - should their size be limited to locals or regionals or interregionals?

Should patronage refunds be paid to non-members as well as members of the cooperative?

Should the evidence of membership in the cooperative be a share of stock or a membership card?

Should a marketing and/or purchasing cooperative elect to qualify for Section 521 of the IRS code (sometimes called exempt)?

Should a cooperative be financed with a majority of equity or debt capital?

Should the membership of a cooperative be open to all or limited in some way?

Should a cooperative price with a margin or at cost of product handled?

Should the membership of a cooperative be free and easy?

Should the cooperative be financed with permanent or revolving equity capital?

What should be the percentage of patronage refunds returned to patrons as cash?

When should an agricultural cooperative use qualified or non-qualified patronage allocations?

Should the objective of the cooperative be to earn profit or provide a service?

Should the voting rights in a cooperative be one vote per member or determined by the amount of business a member does with his cooperative?

You are a member of the Board of Directors of a local Federal Land Bank Association. The manager suggests the Board seriously consider applying for "exempt" IRS status under Subchapter T Section 521. What are the steps the Board should take to prepare to apply for this (521) IRS classification?

You are a member of the Board of Directors of your local Rural Electric Cooperative. A neighbor of yours called on you and complained that since he had to take into his income each year the patronage refund (capital credits) he receives from his Rural Electric Co-op, it has often increased his taxable income enough to put him in a higher IRS tax rate and that the 20% in cash the Rural Electric Cooperative sent was far too little to pay taxes on the total amount of his patronage refund (capital credits) as he and most of his neighbors are in the 40% IRS tax rate. He wants you to have the Rural Electric Cooperative Board raise the cash portion of the patronage refund (capital credits) to 40% or 50% cash. What is your reply to him?

At a Grange meeting you are visiting with one of your neighbors and he asks you what courses you have been taking. Of course, you tell him one of them is "Co-ops". He says that he used to belong to Landmark. In fact, he says that he used to join every year and had always purchased his supplies over at their branch. He goes on to explain that this year they raised their annual membership dues \$5.00 over last year making it \$35 a year. Also, they put on a big campaign in support of a state income tax a few years ago and supported ISSUE I 2 or 3 years ago--neither of which he supported. So he didn't join last year or this. Now he doesn't buy any of his supplies at Landmark but takes all his business over to Joe Blow's Feed Store.

You must now respond to your friend, and you can be frank with him. He respects you. What should you tell him?

In what order of priority should the cash flow of the cooperative be used: 1. To pay dividends on members' capital investment; 2. To redeem old non-cash patronage; or 3. To pay patronage refunds?